United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

ORIGINAL

74-1661

~~74-1699 - 74-1706~~

IN THE

United States Court of Appeals

For the Second Circuit.

FABRIZIO & MARTIN, INCORPORATED,

Plaintiff-Appellee-Appellant,

vs.

BOARD OF EDUCATION CENTRAL SCHOOL DISTRICT NO. 2 OF THE TOWNS OF BEDFORD, NEW CASTLE, NORTH CASTLE AND POUND RIDGE, MARS ASSOCIATES, Inc., and NORBEL CONSTRUCTION CORP. OF NEW ROCHELLE, a joint venture,

Defendants,

THE BOARD OF EDUCATION CENTRAL SCHOOL DISTRICT NO. 2 OF THE TOWNS OF BEDFORD, NEW CASTLE, NORTH CASTLE AND POUND RIDGE,

Defendant-Appellant-Appellee,

AETNA CASUALTY & SURETY CO., Additional Defendant on the Counterclaim of Defendant BOARD OF EDUCATION,

Defendant-Appellee-Appellant.

ON APPEAL FROM A JUDGMENT OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK.

Brief for Aetna Casualty & Surety Company. Defendant

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UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

FABRIZIO & MARTIN, INCORPORATED,

Plaintiff-Appellee-Appellant,

DOCKET NO. 741661

-v-

THE BOARD OF EDUCATION OF CENTRAL SCHOOL DISTRICT NO. 2 OF THE TOWNS OF BEDFORD, NEW CASTLE, NORTH CASTLE AND POUND RIDGE, MARS ASSOCIATES, INC. and NORMEL CONSTRUCTION CORP. OF NEW ROCHELLE, a joint venture.

Defendants-Appellants-Appellees,

THE BOARD OF EDUCATION OF CENTRAL SCHOOL DISTRICT NO. 2 OF THE TOWNS OF BEDFORD, NEW CASTLE AND POUND RIDGE,

Defendant -Appellant -Appellee,

AETNA CASUALTY AND SURETY CO.,

Additional Defendant on the Counterclaim of the defendant, The Board of Education Appellee-Appellant

On appeal from a Judgment of the United States District Court for the Southern District.

ADDITIONAL DEFENDANT APPELLEE'S BRIEF

STATEMENT OF ISSUES

1. WAS THE DISTRICT COURT CORRECT IN DETERMINING THE EQUITITIES VIS-A-VIS AETNA AND THE BOARD IN AETNA'S FAVOR THEREBY FORECLOSING RECOVERY AGAINST THE PERFORMANCE BOND?

2. DID THE BOARD OF EDUCATION COMMIT A FRAUD UPON THE SURETY BY FAILING TO DISCLOSE TO THE SURETY, PRIOR TO THE ISSUANCE OF THE PERFORMANCE AND LABOR AND MATERIAL PAYMENT BOND, FACTS KNOWN TO THE BOARD WHICH GAVE RISE TO THE CONTRACT BEING DECLARED ILLEGAL?

   (A) IS AETNA, AS SURETY, ENTITLED TO DAMAGES?

3. DID THE BOARD OF EDUCATION SUFFER ANY DAMAGE AS A DIRECT CONSEQUENCE OF THE ILLEGALITY?

   (A) ARE BREACH OF CONTRACT DAMAGES A DIRECT CONSEQUENCE OF ILLEGALITY?

   (B) WAS THERE A FAILURE OF PROOF OF DAMAGES BY THE BOARD?

   (C) WERE THE BOARD'S COMPLETION COSTS ILLEGALLY INCURRED PRECLUDING RECOVERY?

   (D) WERE THE COMPLETION COSTS UNNECESSARILY INCURRED?

STATEMENT OF THE CASE

This is an appeal from an opinion and judgment of the District Court for the Southern District of New York dismissing the counterclaims of the BOARD OF EDUCATION CENTRAL SCHOOL DISTRICT NO. 2 of the TOWN OF BEDFORD, NEW CASTLE, NORTH CASTLE and POUND RIDGE ("BOARD") against the plaintiff FABRIZIO & MARTIN, INCORPORATED ("FABRIZIO") and against

AETNA CASUALTY AND SURETY COMPANY ("AETNA") and dismissing the first counterclaim of additional defendant AETNA against the BOARD. (Findings and Opinion of Carter, J. 1055a and Judgment 1074a)

The complaint of plaintiff FABRIZIO had been previously dismissed by order and decision of Ryan, J. (96a).

On or about September 13, 1966, the plaintiff FABRIZIO commenced an action against the BOARD and MARS ASSOCIATES, INC. and NORMEL CONSTRUCTION CORP. of NEW ROCHELLE, a joint venture ("MARS") (10a). The complaint alleged six (6) causes of action seeking to recover damages for various breaches of contract for work performed on the BEDFORD MIDDLE SCHOOL pursuant to a written agreement dated March 17, 1964 between the BOARD and FABRIZIO.

Thereafter, the BOARD moved to stay the action pending arbitration. Judge McLean after conducting a hearing of several days, in an opinion (80a) denied the BOARD's motion on the grounds that the contract which contained the arbitration provision was illegal and therefore the arbitration provision could not be enforced.

On or about August 11, 1967, the Board served and filed its answer (22a) which in substance contained general denials except for two (2) counterclaims (27a-35a). The

fourth defense and counterclaim (27a) sought to recover back all the payments made pursuant to the illegal contract. The fifth defense and counterclaim (30a) sought to recover the BOARD's damages for FABRIZIO's alleged breach of contract.

Thereafter, the BOARD moved to dismiss the complaint and for summary judgment on its counterclaims. FABRIZIO consented to voluntary dismissal of the first, third and fourth causes of action, and Judge Ryan in an order and decision, FABRIZIO & MARTIN, INCORPORATED v. THE BOARD OF EDUCATION CENTRAL SCHOOL DISTRICT NO. 2, 290 F. Supp. 945 (1968)(96a), dismissed the complaint on the grounds that FABRIZIO could not recover on an illegal contract even under the theory of quantum meruit. The BOARD's motion for summary judgment was denied because a trial could only determine whether the BOARD received an "enrichment" which would preclude recovery (117a, 118a). Judge Ryan stated that the BOARD's fifth counterclaim could not stand since it pleads breach of a contract which was declared illegal (118a). Judge Ryan stated that the supplemental agreement could not stand because it depended on the illegal contract (118a). Judge Ryan concluded by stating (118a):

> "In sum, we hold that any claim or defense resting on the illegality of the contract is available to defendant; that it may not plead breach of the prime contract or supplemental agreement or release and waiver under either or failure to present verified claims; and that the issues remaining for determination are the damages which the Board suffered as a direct consequence of the illegal contract, including but not limited to the items enumerated by the Court of Appeals in 'Gerzof'."

The BOARD thereafter commenced an action against AETNA in the Supreme Court of the State of New York by service of a summons. AETNA removed the action to the District Court for the Southern District. On or about March 13, 1969, the BOARD served its complaint (45a). In substance the BOARD alleged breach of the contract and the supplemental agreement by FABRIZIO resulting in delay and liquidated damages in the sum of $520,000.00. The BOARD claimed that by reason of said breaches of contract, AETNA, as surety on FABRIZIO's performance bond was liable to it.

AETNA's answer (56a) contained general denials and the affirmative defenses that AETNA was not liable on its performance bond because the underlying contract was illegal, the supplemental agreement which depended on the

main contract was illegal and could not be enforced, and the affirmative defense of fraud.

AETNA moved to dismiss the complaint on the grounds that it could not be liable on the performance bond because the underlying contract which it bonded was illegal. Judge Wyatt (8a-Filed Opinion #36744) granted AETNA's motion holding that since AETNA did not know of any of the facts relating to the illegality, it could not be liable on its performance bond. Judge Wyatt stated that Gerzof v. Sweeney, 22 N.Y. 2d 297, 292 N.Y.S. 2d 640 (1968) was not applicable to a surety without knowledge.

The BOARD appealed from Judge Wyatt's decision and this Court in its opinion THE BOARD OF EDUCATION CENTRAL SCHOOL DISTRICT NO. 2 v. AETNA CASUALTY & SURETY COMPANY, 453 F.2d 264 (119a), reversed Judge Wyatt's decision and remanded the case, making AETNA an additional party defendant with respect to the BOARD's counterclaim against FABRIZIO. This Court concluded: (128a)

> "Judge Ryan, relying on Gerzof, directed a trial in the Fabrizio-Board action for the determination of 'the damages which the Board suffered as a direct consequence of the illegal contract.' (Fabrizio, supra, 290 F. Supp. at 956). Although this decision removes

> Aetna's premise of no liability under a void contract, it does not establish the nature or extent of the damages, if any, recoverable by the Board against Aetna. Such a determination can only be made after full development of the relating to the underlying equities, vis-a-vis, the Board and Aetna." (emphasis added)

In the pretrial order (130a), the BOARD's first counterclaim was amended to allege delay damages and completion costs resulting from breach of contract in the sum of $496,890.00. The reply of FABRIZIO was amended to allege a defense and setoff claiming there was $708,526.15 still remaining due and owing from the BOARD (131a). AETNA amended its answer to allege a counterclaim in fraud against the BOARD seeking to recover damages in the sum of $169,900.25 (132a, 133a). The BOARD raised no defense to AETNA's counterclaim except in the amendment to the pretrial order to state that the previous decisions of McLean, J., Ryan, J., and this Court precluded recovery (163a).

Carter, J. in a finding and opinion filed on March 27, 1964 (1054a) found that AETNA never had any knowledge of the underlying facts which gave rise to the illegality (1054a); that the BOARD failed to promptly pay

FABRIZIO for work performed or grant extensions of time (1057a); that AETNA had proposed a solution to complete the project but that the BOARD had decided to hire another contractor to complete; (1058a) that the BOARD was primarily responsible for the illegal contract and that the BOARD's conduct justified plaintiff's failure to complete; (1065a). The Court stated (1066a):

> "Applying this standard to the evidence in the immediate case leads me to conclude that the Board cannot recover for the expenses incurred in completing the school. The work stoppage, failure to meet the terms of the contract, the securing of another contractor, and money expended to complete construction were not a direct consequence of the illegal contract. The expenses arose out of breach of the contract by one party or the other, thus foreclosing recovery. Plaintiff cannot be held liable for failure to complete or for breach of a void contract."

In addition, the Court below found that the BOARD was not entitled to recover back the $171,000.00 representing the change order which claim was <u>first raised after</u> the <u>trial</u> (1068a) because the BOARD suffered no damage (1069a, 1070a):

"***Here, however, the damage cannot be said to be $171,000. Unlike Gerzof, the contract here called for a lower, not a higher, price for construction. Moreover, the bid below Fabrizio had been withdrawn because of a miscalculation which would have made it higher than Fabrizio's. The next bid submitted to do the job originally called for was $250,000 greater than the Fabrizio contract price. The public was not really deprived of $171,000 in construction and materials. We can only speculate as to whether and to what extent the altered plans and specifications would have produced savings to the public if the requisite bidding had occurred. What we do know is (1) that the public was not deprived of $171,000 in construction and materials and (2) the value of the unpaid for services, labor and materials received by the Board for which plaintiff seeks recovery of $708,526.15 is far in excess of $171,000 in construction and materials deleted from the original plans and specifications. Since plaintiff is not being allowed to recover for any of these unpaid services, labor and materials, and the public has thereby been enriched to that extent, equity would seem best served by not altering the status quo. Hence, recovery by the Board of $171,000 is denied."

The Court below also concluded that AETNA was not entitled to recover on its counterclaim because it had not been proven that the BOARD had fraudulently concealed the underlying facts regarding the illegal change order (1072a).

STATEMENT OF FACTS

There have been a total of five (5) decisions which relate to the case at bar. In each decision there were certain

findings ot fact and conclusions of law which had a direct bearing on the fifth (5th) decision by Carter, J.

Opinion of McLean, J. (80a)

The opinion of McLean, J., dated July 6, 1967 made findings ot fact which were incorporated in their entirety in the pre-trial order (130a, 135a-143a). Based on the facts presented at a lengthy hearing before him, he declared the contract illegal.

Judge McLean found that the BOARD OF EDUCATION solicited in November 1963, bids for the construction of a school. There were a total of six bidders of which the three lowest were:

Contractor	
Rand Construction Co.	$2,276,800.00
FABRIZIO & MARTIN, INC.	$2,326,900.00
Walter A. Stanley Construction Co.	$2,549,000.00

The contract was awarded to Rand Construction. However, Rand advised the BOARD that it had made a mathematical mistake and the BOARD consented to the withdrawal of the bid.

The next lowest bidder FABRIZIO had also claimed a mistake. The mistake was approximately $171,000.00.

On February 10, 1964, a meeting was held between four (4) members of the BOARD, FABRIZIO, the architect and the BOARD's attorney.

A tape recording was made of the meeting which was introduced into evidence at the hearing before Judge McLean. At

that meeting ways were discussed to eliminate $171,000.00 of work so FABRIZIO could accept the contract.

Judge McLean commenced that the BOARD members had a fair interference that they were violating the bidding statutes: (84a)

> "It is also a fair inference that some of the Board members present had misgivings as to whether such a reduction of the contractor's obligation might not run afoul of statutory competitive bidding requirements. Early in the meeting, the chairman of the Board stated, according to the transcript:
>
> > 'See, we wind ourselves up with the problem that under State law, if we would then take your change of figure here it would then violate the basis upon which we then could grant the contract, because this would mean a change in the overall figures. ***'"

The BOARD's attorney when queried about the illegality was of the opinion that there was nothing illegal about what was happening.

On March 10, 1964, the architect wrote to the BOARD recommending the deletion of certain items of work to cover the error in FABRIZIO's bid.

On March 17, 1964, FABRIZIO and the BOARD entered into a contract for the construction of the school. Simultaneously, the BOARD and FABRIZIO executed a change order which <u>did not</u> set forth dollar amounts (see, 1034a). But Judge McLean found that the items included in the change order were the same as listed in the March 10, 1964 letter but that "no dollar figures were set against any of these items." (88a)

Judge McLean found that the change in the plans and specifications and the change order were not submitted to the State Education Department for approval until June 1967, three (3) years later, and just prior to the hearing before him.

Judge McLean also noted that the facts relating to the illegal change order, namely the March 10, 1964 letter (defendant AETNA's Exhibit "B" in evidence) were hidden by the BOARD (89a):

> "The former clerk of the Board testified that on March 17, 1964, the assistant superintendent of schools instructed him to see to it that copies of this letter of March 10, 1964 were removed from the files of the school district."

Thus, Judge McLean adduced from the foregoing facts that the contract between the BOARD and FABRIZIO was illegal because it violated Section 103 of the General Municipal Law.

Opinion of the United States
Court of Appeals (119a)

The BOARD appealled from the prior decision of Judge Wyatt, which dismissed the BOARD's complaint against AETNA.

On that appeal, in Point I of the BOARD's Brief on Appeal, p. 11, the BOARD argued that pursuant to an affidavit of one Charles W. Fowler (page 106a of the prior record) submitted on the motion before Judge Wyatt, the AETNA had knowledge of the facts of the illegality (pages 5 and 6 of the BOARD's Brief on Appeal) prior to entering into the supplemental agreement. Also on that appeal, the BOARD contended that AETNA refused to complete after FABRIZIO's contract was terminated.

The Court in reversing Judge Wyatt, relied upon certain facts which at the trial on the merits proved to be without basis in fact and completely erroneous, namely, that this Court assumed that AETNA had knowledge of the illegality at the time AETNA consented to the supplemental agreement and that AETNA had refused to complete the work after FABRIZIO's contract was terminated.

This Court in reversing the lower court's decision, and remanding the suit for trial made AETNA an additional defendant on the BOARD's counterclaim, ordering consolidation with the pending FABRIZIO-BOARD action "so that all the facts bearing upon the rights of the parties may be adduced." (129a)

The Court did not state that AETNA was absolutely liable for damages. To the contrary, this Court stated (128a):

> "Although this decision removes Aetna's premise of no liability under a void contract, it does not establish the nature or extent of the damages, if any, recoverable by the Board against Aetna. Such a determination can only be made after full development of the facts relating to the underlying equities, vis-a-vis the Board and Aetna." (emphasis supplied)

We submit that had this Court had before it the facts adduced at trial before the District Court below, it might have reached a far different conclusion.

POINT I

THE EQUITIES WERE IN AETNA'S FAVOR

The Court below in its opinion after trial concluded that the following basic facts were incontrovertible:

"Aetna signed as surety on a performance bond in respect of the March 17, 1964 agreement, but it had no knowledge of the agreement between the Board and Fabrizio to violate Section 103 of the New York General Municipal Law by altering the plans and specifications in order to enable Fabrizio to do the work at its original bid price. A year later on March 23, 1965 a supplemental agreement was entered into by the Board and Fabrizio. Aetna again was surety on a performance bond in respect of this agreement. Aetna was unaware of the transactions and agreement which rendered the contract, performance of which it was guaranteeing, void and unenforceable until institution of this action." (1057a)

"***On April 15, 1966 the Board, Fabrizio and Aetna met to seek to determine whether their differences could be ironed out. Aetna proposed a solution and Fabrizio agreed that if that solution was acceptable, it would complete construction by July, 1966. The Board, however, decided to secure another contractor to complete construction and awarded the contract to complete construction to Mars Normel." (1058a)

The record of the trial is replete with testimony and exhibits which not only support the Court's conclusion but show that the scale of equity weighs heavily in AETNA's favor.

The BOARD's own witness, the same Charles W. Fowler, who submitted an affidavit in opposition to the AETNA motion for summary judgment claiming that AETNA had knowledge of the illegality, changed his tune. Mr. Fowler testified that on the same date as the execution of the contract between the BOARD and FABRIZIO he wrote to the BOARD's President questioning the legality of the contract (637a). The letter, dated March 17, 1964, was read into the record (638-639a). Mr. Fowler refused to release the BOARD's seal to be affixed to the contract because

he was aware that the contract would be illegal. Then, Fowler testified that the March 10, 1964 letter written by the architect to the BOARD's attorney, outlining the items which would be included in the illegal change order were ordered removed from the records of the BOARD and ordered destroyed (642a.) This is substantiated by a memorandum (Defendant's Exhibit "B" in evidence) which was written by the same Mr. Fowler outlining the chronology of the events up to January 1, 1966. It clearly shows more than a mere suspicion by the BOARD that it was acting illegally. It shows an absolute awareness that what was being done was illegal. The BOARD did not disclose any of this to AETNA or make FABRIZIO aware of the question of legality. Mr. Fowler further testified that he did not send the March 10, 1964 or the March 17, 1964 letter to AETNA (642a). Mr. Fowler testified to his knowledge that no one from the BOARD ever advised AETNA of the facts relating to the illegality (643a) or even gave any consideration to notifying AETNA of any of the facts relating to the illegal change order (643a). Mr. Fowler testified that as Clerk of the BOARD he never notified AETNA subsequently of the underlying illegal facts surrounding the execution of the contract and the change order (643a). Mr. Fowler further admitted that the BOARD never notified AETNA or sent the contract and change order to AETNA (643a-644a). Mr. Fowler admitted to the Court that none of the underlying facts which let to the illegality were ever made known to the

SCHOOL BOARD until the trial before Judge McLean (645a), i.e., June, 1967, more than three years after the contract was originally entered into and after the completion of the entire project.

AETNA's own witnesses further substantiated that AETNA never had knowledge of the facts of the illegal change order.

Clifford O. Christensen, the AETNA bond manager testified he did not know the underlying facts which gave rise to the contract being declared illegal and had never seen Mr. Fowler's March 17, 1964 letter (824a, 825a).

Thomas P. Moyna from AETNA's New York office, the underwriter who executed the performance bond, as well as the payment bond, testified that he had no knowledge of the circumstances which gave rise to the contract being declared illegal or the facts set forth in Mr. Fowler's March 17, 1964 letter (827a, 828a).

AETNA's supervisor of the Bond Underwriting Department, Richard B. Pratt, testified that neither he nor the underwriting department had any knowledge of the facts which gave rise to the contract being declared illegal and void at the time he authorized the writing of the bonds (830a).

Even after disputes arose between the BOARD and FABRIZIO, at subsequent meetings, the BOARD never disclosed to any of AETNA's claim personnel or AETNA's attorney any of the underlying facts relating to the illegality even though these meetings took place one and two years later. (Harold Wareham, 848a; John Wiley, 854a; Max E. Greenberg, 873a, 884a)

AETNA was not present at the contract signing when the performance bond was delivered. (Vincent Fabrizio, 997a, 998a) AETNA was not present at the secret meetings which were taped. (Vincent Fabrizio, 971a, 972a)

The clear lack of knowledge on the part of AETNA of the underlying facts is commented on by the Court and conceded by the attorney for the BOARD during the trial (834a, 835a):

"THE COURT: I think it is clear, as far as I can see, that Aetna didn't know about it, in any event.

MR. YAVNER: We are conceding nobody knew about it until Judge McLean made a ruling.

THE COURT: I don't think that is true. The question is whether or not it is or may be a legal obligation, you can say. But the Board certainly knew that what it did and Fabrizio certainly knew what the Board did. It may well be that you did not understand the effect of what you did but you certainly knew.

Aetna is arguing that those facts that you knew about and the way that you accomplished execution of this contract you did not reveal that to them. That is what the arguement is. Not the fact of what you did. You knew the assignment that you made, the bid you took, that you made a simultaneous change order and so forth and so on. You knew that.

MR. YAVNER: There is no question about that. There is no challenge about that. If he asks for a concession I will concede that without the witnesses. But my position on the questions he is putting, the reason for my objection,

is because the underlying facts were known to lawyers. There was a Board counsel at that time. He advised the Board. There is a question of the legal effect to ask these witnesses whether they would enter into this thing --

THE COURT: Did Aetna's lawyers know ho you found out about that contract? That is the point. You knew about it. Mr. Yavner.

MR. YAVNER: I didn't know about it.

THE COURT: The Board's lawyers knew about it and Mr. Powers started out indicating that Fabrizio was innocent because he had no lawyer at these various conferences and so forth so that he is saying that although he knew the facts he was not aware of the legal facts.

Aetna says that their lawyers did not know anything about it.

Obviously, if Aetna had known the facts, it would probably have discussed those facts with its attorneys."

Thus, the attempt by the BOARD to infer knowledge by setting forth the supplemental agreement on pages 9 through 11 of its brief is specious. Especially when the BOARD's counsel conceded at the trial the fact that AETNA had no knowledge of the underlying facts giving rise to the illegality.

The BOARD's actions after the final and wrongful termination of the FABRIZIO contract is consistent with the complete bad faith exercised throughout the entire relationship. AETNA

attempted to have the entire project completed without additional cost to the BOARD, subject only to a reservation of rights of all the parties to be determined after the completion of the project. (Max E. Greenberg, 870a-874a) The BOARD's attorney during the cross-examination of the witness (Max E. Greenberg, 875a-885a) conceded such a proposal by AETNA and for some unknown reason went out and got another contractor.

Thus, the BOARD rather than mitigating the loss embarked on a course of needless expense when AETNA offered to complete with its financial resources.

This is the very same BOARD which now cries out and contends that the public purse must be safeguarded.

This Court asked the District Court on a trial of the merits to balance the equities, vis-a-vis AETNA and the BOARD. It is clear and undisputed that the BOARD knew, contrary to any attorneys advise, that it was acting improperly and attempted to hide illegality and its misdeeds by destruction of records. It is further clear and undisputed that AETNA at all times acted properly and fairly while the BOARD's bad faith permeated the entire devious and tragic debacle.

The substantive law of New York is clear that an innocent surety is not liable on its performance bond. Village of Medina v. Dingledine, 152 App. Div. 307, 136 N.Y.S. 786 (4th Dep't. 1912), aff'd. 211 N.Y. 24, 104 N.E. 1118 (1914). Nor has the BOARD to date cited one New York case which has held

to the contrary. To hold to the contrary would compel an innocent party to contribute damages to a wrong-doer which is not only inequitable but totally unjust under any system of jurisprudence.

In the Village of Medina, supra, at page 791, it was stated:

> "... Even conceding that plaintiff could waive as to it its right to insist for that reason that the contract was void, and could consent that the contractors might continue their illegal manner of its performance, yet this concerted action by plaintiff and the contractors, of which the Surety Company had no knowledge, or notice, and to which it was in no way a party, could not alter, or impair, its rights, or enlarge or change, its obligations as surety. The contract, performance of which it had guaranteed, was one to be performed in accordance with the statutory requirements. When these provisions were with plaintiff's tacit consent continuously disregarded and violated by the contractors, then, as to the Surety Company, the contract became and was void, and no liability for nonperformance of the contract remained; for, as to it, there was no longer any contract to which its guaranty of performance could apply." (emphasis supplied.)

Similarly, in Kent v. Thornton, 179 Misc. 593, 39 N.Y.S. 2d 435, 443 (S. Ct. Chautauqua Co., 1942) aff'd. 265 App. Div. 904, 38 N.Y.S. 2d 573 (4th Dep't 1942), it was held:

> "This conclusion disposed of this litigation except for the bond given by Charles for the performance of the contract. The bond, however, having been given for the performance of a contract which was never a valid enforceable contract, cannot be made the basis of a recovery of damages."

C.J.S., Vol. 72, Principal and Surety §14, states the same sound rule:

> "The obligation of the principal for the payment or performance of which the surety undertakes to make himself collaterally liable, must be a valid and binding obligation as between the principal and the creditor or obligee. It it is invalid the surety, as a general rule, will not be bound, especially where he had no knowledge of its invalidity at the time he became surety, and even though he believed it to be valid. * * *"

There have been other jurisdictions which follow New York law.

In Metz v. Warrick, 217 Mo. App. 504, 512, 269 S.W. 626, 627 (1925), the surety had given a contractors bond to the SCHOOL DISTRICT. The contractor and the SCHOOL DISTRICT had entered into an oral contract in violation of the state statutes. It was held that although the contractor was liable, the sureties were not liable on their bond:

> "The sureties on his bond, however, are not estopped to assert that there was no contract between Warrick and the school district. The bond which they signed was given to guarantee the performance of a contract between Warrick and the school district and since there was no such contract, there was no consideration for the bond. A want of consideration may be shown to avoid any contract when there is no question of an innocent holder or purchaser involved. The bond in this case was given to the school district to guarantee the performance of a contract by Mr. Warrick, but when it developed that there was no contract between Warrick and the School District, then, in the very nature of things, the sureties on the bond could not be bound to guarantee the performance of a

contract that did not exist. The supposed contract between Warrick and the school district was void ab initio and not merely voidable, and since it had no validity, the bond given to secure its performance had no validity. For that reason the plaintiff had no remedy against the sureties on this bond, and as to them the judgment was for the right party." (emphasis supplied.)

Pittsburgh Const. Co. v. West Side Belt R. Co., 154 F. 929, 933 (3d Cir. 1907) held as follows:

"The suit here is against the sureties of the contractor and the illegal contract the basis of the action. As the plaintiff must rely upon its void contract to recover, the action must fail. The test as to whether the action is grounded upon the void contract depends upon whether it requires the aid of an illegal transaction to establish the case, and, if it be necessary to prove the illegal contract in order to maintain the action, the courts will not enforce it, nor will they enforce any alleged rights springing from such agreements ***". (emphasis supplied)

In Cameron County Water Improvement Dist. No. 8 v. De La Vergne Engine Co., 93 F.2d 373, 376 (5th Cir. 1937); aff'd. 100 F.2d 523, the water district illegally paid for certain equipment by the issuance of a note without a taxpayer vote authorizing such an indebtedness as required by statute. An individual surety guaranteed the indebtedness. The Court held no liability on the part of the surety:

"...When the primary obligation of the district fails, because the contract of purchase was in excess of its powers and contrary to positive law, the liability of Berreda as an indorser or surety fails with it. (cases and authority cited)"

and quoting Miller v. Stewart, 22 U.S. (9 Wheat) 680 (1824)

> "Nothing can be better settled, than the doctrine that, if an obligation be dependent on another obligation (and, by parity of reasoning, upon the legal existence of another instrument, and the latter be discharged, or become void, the former is also discharged. Sheppard in his Touchstone (p. 394), puts the case, and illustrates it, by adding, 'as if the condition of an obligation be, to perform the covenant of an indenture, and afterwards the covenants be discharged, or become void; by this means, the obligation is discharged and gone forever.'"

Point V of the BOARD's brief (ppg. 36-43) attempts to cite authority for the proposition that in New York, a surety remains liable on the performance bond even though the contract is declared illegal and the surety was without knowledge of the facts giving rise to the illegality and in no way participated in the illegal transaction. Does the BOARD cite one New York case as authority for its contention? Instead the BOARD cites authority from other jurisdictions or misstates the authority cited.

Restatement of Contracts, §601, illustration 2, cited by the BOARD, deals with a party who participated in the illegality and guaranteed or furnished the bond, a far cry from the case at bar. The BOARD concedes that AETNA was without knowledge of the illegality. (834a, 835a)

In People's Lumber Co. v. Gillard, 136 Cal. 55, 68 Pac. 576 (1902) the BOARD has been deliberately misleading. (p. 37)

In Gillard, (supra), the suit was not on a performance bond but by a supplier of material to the principal on the labor and material payment bond. Furthermore, in Gillard (supra), the Court further inferred that the sureties had knowledge of the facts which is not the case at bar. There is no dispute that an illegal prime contract does not taint the subcontract or the payment bond which is in issue in the Gillard case (supra). But, the suit in this case is on a performance bond. The illegality did not taint the payment bond, and AETNA paid many laborers and materialmen of FABRIZIO.

City of Madison v. American Sanitary Engineering Co., 118 Wisc. 480, 95 N.W. 1097 (1903) relied upon by the BOARD at page 38 of its brief is not applicable. Furthermore, it is not New York law. The contractor had entered into a contract with the City for the construction of a sewage treatment plant. Pursuant to said contract, a performance bond was given to guarantee the faithful performance of the contract. The sewage disposal plant was completed and pursuant to the contract, the contractor operated same for three (3) months. The plant was tendered to the City who refused to accept operation since the City claimed that it was not operating properly. Finally, after the contractor had made certain changes in the operation of the plant, the City took charge of the plant. However, the plant did not function properly

and the City sued the contractor and the surety for breach of contract. The Court decided in favor of the City and against the contractor and surety for the failure of the plant to operate as guaranteed. Contrary to the Board's contention, the Court did not find the contract illegal and void, but that the contract was breached. The surety did raise other defenses of material alterations to the contract in granting extensions of time and payments to the contractor which the Court disposed of unfavorably to the surety. The Court did indicate by way of dictum that the surety in the first instance could not attack the contract by claiming illegality. This is not the case at bar. The contract has already been declared illegal in a separate action. Secondly, the contract in City of Madison (supra), was a completed contract.

The BOARD's reliance on Phoenix Assurance Company of New York v. City of Buckner, Mo., 305 F.2d 54 (8th Cir.), cert. denied 371 U.S. 903 (1962) is again misplaced. Not only is this case not New York law but also has no relevance. In Phoenix (supra), the contract was not declared illegal and void. The surety had contended that the contract was void because the City didn't have the funds to pay the contractor at the time of the furnishing of the bond, unreasonable delay in notifying the contractor to proceed, assignments to creditors by the contractor, increases in prices for labor and material, and that the original contract was abrogated and there was a new

contract.

The BOARD attempts frivolously on pages 40-42 of its Brief to circumvent Judge Ryan's decision by contending that the supplemental agreement did not fall because the primary contract was illegal. Judge Ryan was correct when he stated: (118a)

> "Insofar as the Fifth counterclaim seeks damages flowing from breach of the prime contract and supplemental agreement by plaintiff, it cannot stand: the prime contract, because it has been illegal; the supplemental agreement because it depended for its existence on the continued validity of the prime contract. ***"

The BOARD contends that this was a new agreement with new consideration. If this be so, then it would violate the public bidding statutes, General Municipal Law §103. The BOARD contends this is not so because it had the powers to enter into the supplemental agreement pursuant to Section 1709, subd. 33 of the Education Law. Subd. 33 states:

> "To have in all respects the superintendance, management and control of the educational affairs of the district, and, therefore, shall have all the powers reasonably necessary to exercise powers granted expressly or by implication and to discharge duties imposed expressly or by implication by this chapter or other statutes."

On its face, Section 1709, subd. 33 of the Education Law is not applicable. Thus, the BOARD has been misleading again.

Nor was there any new consideration or a new independent agreement. The BOARD's reliance on 10 N.Y. Jur., Contracts,

§173 and §174 is misplaced. Section §173 states:

> "Where an agreement grows immediately out of, or is connected with, an illegal or immoral act or agreement, a court cannot lend its aid to enforce it, though it is in fact a new agreement. If the connection between an original illegal transaction and a new promise can be traced, if the latter is connected with, and grows out of, the former, no matter how many times and in how many different forms it may be received, it cannot form the bases of a recovery. ***"

10 N.Y. Jur., Contracts, §174 cited by the BOARD is equally inapplicable. This section deals with exactly what has been said before. Third parties can recover since the illegality does not taint their contractual right of recovery. This is not the case at bar. The BOARD, who participated directly in the illegality and whose contract and supplemental agreement is illegal, chooses to use these agreements to prove liability on AETNA's part.

The BOARD's counsel offered the supplemental agreement (1036a) into evidence for a limited purpose. Counsel for the BOARD stated that the supplemental agreement could not be the basis of a claim for damages (694a-695a). It was only offered into evidence to show that based on the underlying facts, it was no better than the basic contract which was declared illegal. In other words, the basic contract was illegal and could not be the basis of a recovery. So too, the supplemental agreement could not be the basis of a recovery: (694a-695a)

"MR. YAVNER: My next offer is of the supplemental agreement which is not in evidence and I am not offering it for any relationship to damages we expect against them now, the liquidated damages or the like, but because it sets the underlying stage in the same way that the first exhibit, the basic contract between the two does. It also does set the basic contract with Aetna in perspective as well.

Only for that purpose do I offer this in evidence now."

The BOARD has now taken a completely contrary position. However, the foregoing admission by the BOARD during the trial is fatal to any contention by the BOARD that the supplemental agreement germinated any liability on the part of AETNA.

POINT II

THE BOARD COMMITTED A FRAUD UPON AETNA WHICH ENTITLED AETNA TO DAMAGES

AETNA had no knowledge of the underlying facts which gave rise to the illegality. This was conceded by the BOARD's attorney during the trial (834a) and further supported by the testimony of Mr. Fowler, Clerk of the BOARD (642-643a) and AETNA's Exhibit "B" in evidence.

The BOARD was silent and failed to disclose these

underlying facts. The question is asked whether the BOARD had a duty to disclose the facts.

The Court below stated that "at best the BOARD's knowledge of illegality was equivocal making failure to disclose it insufficient to establish fraud." (1072a)

The District Court had concluded that AETNA had made little effort to discover the facts and that the BOARD was relying upon the advice of counsel.

The District Court position is inconsistent with its previous finding of fact that AETNA never had knowledge of any of the underlying facts which gave rise to the illegality (1057a). AETNA had no reason to be suspicious of any irregularity because as the Court stated, the contract was awarded at the original bid price (1056a). This was also confirmed by Richard B. Pratt when he testified that the award and contract price stayed the same. Thus, there was no reason for AETNA to inquire and AETNA had a right to assume that the BOARD and its principal had entered into a proper contract. Bank v. Board of Education of the City of New York, 305 N.Y. 119, 133, 111 N.E. 2d 238, 244 (1953). AETNA had a right to presume that the BOARD as a public body had performed its duties according to law. 21 N.Y. Jur., Evidence, §111. Thus, there was no duty to inquire by AETNA. To the contrary, it was incumbent upon the BOARD to disclose that the contract had not been awarded under the usual circumstances.

Nor can it be stated that the BOARD didn't know that it was doing something wrong. Why order the removal and destruction of records relating to the illegal change order if counsel had advised that it was a legal contract? (642a) AETNA did in fact rely upon the fact that the contract was legal. Richard B. Pratt, a bond underwriter who had thirty-five (35) years previous experience (837a) stated that he had never written a bond where the facts were similar to the instant case (837a, 838a) and who after reviewing the findings of fact by Judge McLean which were set forth in the pretrial order (135a-143a), clearly stated that he would not have written the performance bond and payment bond, it he knew those facts or the facts set forth in Mr. Fowler's March 17, 1964 letter. (838a)

It is unimportant whether or not AETNA's principal disclosed any of the facts. What is important is whether the BOARD disclosed any of the facts which it conceded it did not do. Damon v. Empire State Surety Company, 161 App. Div. 875, 146 N.Y.S. 996, 997 (2d Dep't., 1914):

> "The plaintiffs, prior to the acceptance of the bond, had no direct dealings with the defendant. It was the machine company that applied for the bond. The machine company was not the agent of the plaintiffs, and they are not bound by any fraudulent representations in which they did not participate, or which were made without their knowledge. Western N.Y. Life Ins. Co. v. Clinton, 66 N.Y. 326; Ludekens v. Pscherhofer, 76 Hun, 548, 28 N.Y.

> Supp. 230; Howe Machine Co. v. Farrington, 82 N.Y. 121; Powers v. Clarke, 127 N.Y. 417, 28 N.E. 402. At the same time it is well recognized that the obligee, before accepting the bond of the surety, is called upon to make such disclosures of facts within his knowledge, of which the concealment would amount to a suppresio veri, and thereby become fraudulent, and it is not necessary that this concealment should inure to the benefit of the obligee, provided it operates to the prejudice of the surety."

It was stated in 57 N.Y. Jur. Suretyship and Guaranty, §101:

> "Fraud on the part of the obligee such as will avoid a contract of suretyship is not confined to positive affirmations which are untrue, but may consist in the concealment or withholding by the obligee from the surety at the time the contract of suretyship is executed of material facts affecting the risk, where the obligee had the opportunity, and duty to disclose. Although the statement may be too broad, and is subject to the qualifications discussed below, it has been said that the creditor's duty to deal with the surety in utmost good faith in every step of the transaction requires the creditor to disclose fully every point which is likely to bear upon the surety's disposition to enter into his undertaking. Before accepting the undertaking of a surety, the obligee certainly has a duty to disclose facts within his knowledge the concealment of which amount to a suppression of a material fact and therefore become fraudulent."

The District Court erroneously relied upon Mohasco Industries, Inc. v. Griffen Industries, Inc., 335 F. Supp. 493 (S.D.N.Y. 1971) for the proposition that AETNA had failed to make further inquiry concerning the illegality. In

Mohasco (supra), the guarantor already knew the underlying facts prior to issuing the guaranty but failed to make further inquiry. In the case at bar, all the facts of the illegality were concealed so that AETNA could not be put on notice that there were unusual circumstances which required further inquiry.

In Kennedy Electric Co., Inc. v. United States Postal Service, 367 F. Supp. 828, 829 (D. Colo. 1973), the following was stated:

> "One has the right to assume, in the absence of reasonable grounds to think otherwise, that other persons will obey applicable laws and regulations, and one is not negligent in failing to anticipate that the other persons may violate such laws and regulations."

It has been generally stated that fraud has a great many definitions, and depends upon the circumstances and the relations of the parties. Cowles v. Board of Regents of University of the State of New York, 266 App. Div. 629, 44 N.Y.S. 2d 911 (1943), aff'd. 292 N.Y. 650, 55 N.E. 2d 515 (1944). Supported by the facts in the case at bar, it has been said that fraud is synonymous with overreaching, that is, taking of unfair advantage to another's detriment by deceitful or unfair means and in the final analysis, conduct inconsistent with fair dealing and good conscience. People v. S. W. Straus & Co., Inc., 158 Misc. 186, 285 N.Y.S. 648 (1936), mod. on other grounds, 248 App. Div. 785, 289 N.Y.S. 209 (1936); In Re Denny's Estate, 5 Misc. 2d 475, 160 N.Y.S. 2d 722 (1957); In Re Alfaya's Will, 122 Misc. 771, 204 N.Y.S. 90 (1924), aff'd. 213 App. Div. 877, 209, N.Y.S. 785 (1925).

The Circuit Court of Appeals, in reversing the trial court's granting of AETNA's motion for summary judgment and remanding for trial, stated (128):

> "***Although this decision removes Aetna's premise of no liability under a void contract, it does not establish the nature or extent of the damages, if any, recoverable by the Board against Aetna. Such a determination can only be made after full development of the facts, relative to the underlying equities, vis-a-vis the Board and Aetna." (emphasis ours)

On that score, it is said that fraud in equity is infinite and that in this forum many acts, transactions or circumstances are considered fraudulent which would not necessarily be so regarded at law. Jackson ex dem. Cadwell v. King, 4 Cow. 207 deals with those manifold varieties of fraud where relief is required for the purpose of substantial justice. Re Dorrity, 118 Misc. 725, 194 N.Y.S. 573 (1922).

DAMAGES

The New York Rule on the measure of damages for an action in fraud is stated in Reno v. Bull, 226 N.Y. 546 (1919)and is called the "Out of Pocket Loss" Rule. The Court in Reno (supra), stated at page 553:

> "The true measure of damage is indemnity for the actual pecuniary loss sustained as the direct result of the wrong..."

Included in the item of damages can be legal fees if the wrongful act occasioned the fees; Fugazy Travel Bureau, Inc. v.

Ernst & Ernst, 31 A.D. 2d 924, 298 N.Y.S. 2d 519 (1st Dep't., 1969); and legal fees may be recovered where the wronged party is defending against the wrongdoer who is seeking to enforce the fruits of his fraud. Gantell v. Friedmann, 197 N.Y.S. 2d 605 (1959). Also counsel fees suffered in defending actions by third parties to enforce a liability which resulted from the fraud is recoverable. Hynes v. Patterson, 95 N.Y. 1 (1884).

(a) Payments Under the Labor and Material Payment Bond

AETNA's witness, Michael J. Buckmir, stated that he was a claim representative who received claims from various labor and materialmen (885a); that as a claim representative he conducted an investigation of the claims (859a). In making payments, he referred to the labor and material payment bond as a guide to determine whether it was an obligation under the bond (862a-863a). The witness stated that there were 51 claimants. To verify the claims the witness stated that he checked the principal's records thoroughly (863a), contracted the claimant, and if a claimant was a subcontractor, checked the subcontract, checked billings, ledger sheets and payment sheets (863a-864a). The witness stated that payment was made by company drafts, that he had each draft and each draft had been negotiated by the payee (864a). The witness testified that he had prepared a schedule of the claimants listing the amount that had been

paid to each claimant (859a). The witness stated that the total amount of claims paid were $114,609.58 (865a). Rather than put all the claim files and drafts into evidence, it was stipulated that the schedule be submitted into evidence with the exception of four items on the list, which were numbered 45, 46, 47 and 48 (888a-891a). The schedule was received into evidence as defendant AETNA's Exhibit "D" (891a). Counsel for defendant BOARD objected to the inclusion of these four (4) items because they were payments for Union Welfare and Pension Funds (890a).

As to these four items, in the sum of $523.00, $594.17, $956.00 and $58.10 (Exhibits "E", "F", "G" and "H" in evidence, (898a), the witness stated that on the advice of his home office and legal advice from counsel, he paid the claims under the payment bond (893a). Counsel for defendant BOARD objected to their introduction into evidence since he claimed that they were not payments to or on behalf of a subcontractor. However, counsel for defendant BOARD missed the point. The question is whether this was a legal obligation under the payment bond which the BOARD fraudulently induced AETNA to write. It makes no difference who the claimant is. The law is quite clear in New York that Union Welfare and Pension Funds are valid claims against a labor and material payment bond. Martin v. William Casey & Sons, Inc., 5 A.D. 2d 185, 170 N.Y.S. 2d 228 (1st Dep't., 1958).

Thus, additional defendant AETNA submits it has substantiated its payments in the sum of $114,609.58 under the payment bond. (Defendant's Exhibit "D" in evidence)

(b) Payment of Legal Fees

The payments of legal fees are broken down into two (2) categories.

(1) The first category are those fees which AETNA paid in defense of the action by the defendant BOARD on the performance bond which waswritten as a result of the fraudulent concealment. The first legal fee paid in defense of the BOARD's claim was Defendant's Exhibit "J" in evidence (905a). The bill was for legal services for the period of March 30, 1966 to April 5, 1968 in the sum of $20,353.65, of which $20,000.00 represented counsel fees and $353.65 in expenses (903a). Part of Exhibit "J" was an itemized sheet listing each date and amount of the expense. Also attached to the bill for legal services was an itemized statement, twenty-four pages long, listing a schedule of services rendered each day and the service that was performed. Also attached to the bill was the draft of payment.

Defendant's Exhibit "N" in evidence (907a), consisted of four (4) bills for services rendered in the instant action from March 7, 1968 to January 3, 1973. The first bill was for the period of March 7, 1968 through May 13, 1970, and was for

$10,800.00 legal services and disbursements of $298.84 for a total of $11,098.84. The bill was a twelve (12) page statement itemizing services performed on each day in that period of time. The draft of payment was attached to the bill. The second bill was for the period of May 12, 1970 through April 12, 1972, and was for legal services valued at $11,903.50 plus disbursements of $181.05, for a total sum of $12,084.55. This bill included an itemized statement sixteen (16) pages long, giving a daily detailed breakdown of the services rendered. The draft of payment was annexed to the bill. The third bill was for services rendered from April 13, 1972 through July 28, 1972 and was for services in the sum of $7,554.02. This bill contained a three page daily breakdown of the services rendered. The fourth bill was for services rendered from August 10, 1972 through January 1, 1973 in the sum of $5,869.00 plus disbursements in the amount of $145.35, for a total bill of $6,014.35. This bill also contained a daily breakdown of services rendered and was four (4) pages long.

In addition, there were two (2) other expenditures by additional defendant AETNA, in the sum of $26.25 for a court reporter and $473.07 for the copies of appeal briefs (Defendant's Exhibit "O" in evidence, 907a).

The total out-of-pocket expenses to AETNA in defending this action was the sum of $57,604.73.

(2) The second category of legal expenses incurred was in the defense of various claims against the labor and material payment bond.

Defendant's Exhibit "I" in evidence (903a), was a bill dated January 15, 1969, for services rendered in the successful defense of an action by a creditor seeking to recover the sum of $115,903.43. The bill consisted of a twelve (12) page itemized statement listing all disbursements and each day's services from February 8, 1968 through December 27, 1968 totalling 294 hours of attorneys' time. The bill was for $12,500.00, plus disbursements of $488.20, for a total sum of $12,988.20. The draft of payment was annexed to the Exhibit "I".

The same creditor, San Marco, started a second suit in the sum of $34,000.00 and a separate bill dated June 22, 1971 was rendered in this suit for $500.00 plus disbursements of $42.39 for a total bill of $542.39. The action is still pending. The bill (Defendant's Exhibit "L" in evidence, (906a) states that at the time of the bill, 16 hours of attorneys' time was expended. Draft of payment was annexed to the Exhibit "L".

The creditor San Marco started a third suit based on the same facts as the first action and Exhibit "M" (in evidence, 906a), is for legal services and disbursements in the successful dismissal of that action. The bill was for $520.00 and states that 18 hours of attorneys' time was expended. The draft of

payment is annexed to the bill.

Exhibit "K" in evidence (906a) was a draft and a bill for services rendered in the defense of a suit by a subcontractor by the name of Arrow Louver. The statement incorporated in the bill states that the action is still pending. The bill plus disbursements was for $587.30.

Exhibit "P" in evidence (913a) consisted of five (5) additional payments for legal fees. The first draft was in the sum of $2,078.42, payable for legal services in the defense of a claim by Ceco Corporation (910a), a claimant appearing on the schedule (Defendant's Exhibit "D" in evidence 891a) ultimately paid $15,941.50. Also, there was a dratt for legal services in the sum of $971.02 incurred in the defense of the Leonard Adams Company, a claimant paid the sum of $9,000.00 (914a) during trial with the assistance of the Court. The bill was dated June 3, 1970 and was annexed to Defendant's Exhibit "O", in evidence (907a). The bill covering the Adams fee contained an itemized statement of services rendered. Also attached to Defendant's Exhibit "P" in evidence was a draft in the amount of $1,324.89 for legal services in defending a suit brought by claimant Korok, listed on Defendant's Exhibit "D" in evidence as a suit successfully defended. Another draft for legal services was for $2,662.87 for the defense of an action in the sum of $7,655.00 brought by claimant Bradhurst Site Construction Co., which was also successfully defended

(912a). The last draft for legal services was in the sum of $308.81 in the defense of an action brought by a claimant named Accessory Specialties.

The witness (Buckmir) repeatedly stated that the payments for legal services were as a result of legal expenses incurred in the defense of claims against the labor and material payment bond.

The total out-of-pocket expense by additional defendant AETNA in defending claims by subcontractors on the labor and material payment bond, was the sum of $21,012.88.

Thus, the total damages which the additional defendant suffered because of the fraudulent concealment, none of which would have been incurred if such a concealment had not occurred is the sum of $193,227.19, which it seeks in its counterclaim. For AETNA would not have written the bonds if it had known of the facts concerning the execution of the contract.

The BOARD failed to state in the pretrial order (163a) or raise any defense during the trial to AETNA's claim for damages except to state that the previous decisions precluded recovery. It was only in a post trial memorandum that the BOARD claimed that AETNA failed to file a Verified Claim pursuant to §3813, subdivision 1 of the State Education Law.

There can be no question but that an action based on

fraud is grounded in tort and is governed by the provisions of §3813, subdivision 2, of the State Education Law, if applicable at all. A careful reading of §3813, subdivision 1 of the State Education Law renders the BOARD's contention inapplicable to the case at bar. Section 3813(2) reads in part as follows:

> "Notwithstanding anything to the contrary hereinbefore contained in this section, no action or special proceeding founded upon tort..."

Furthermore, defendant BOARD's contention as to failure to present a verified claim pursuant to §3813, subdivision 1, of the Education Law, was dealt with and effectively eliminated by Judge Ryan's decision on defendant BOARD's motion for summary judgment,290 F. Supp. 945, (118a) as follows:

> "In sum, we hold that any claim or defense resting on the illegality of the contract is available to defendant; that it may not plead breach of the prime contract or supplemental agreement or release and waiver under either or <u>failure to present verified claims</u>; ..." (emphasis ours)

Courts have recognized the distinction between the pleading and notice requirements of Sections 1 and 2 of the State Education Law as recently as March 1973 in the case of <u>Double M Construction Corp.</u> v. <u>Matter of Central School District #1, Town of Highlands</u>, 41 A.D. 2d 771, 341 N.Y.S. 2d 905 (2nd Dep't. 1973).

As distinguished from Section 1 of §3813 of the Education Law, Section 2 does not require the allegation in a

complaint that a written verified claim upon which such action is based be presented to the governing body of the District within three months of accrual of such claim.

The failure to comply with §2 of 3813 of the Education Law however is an affirmative defense to be raised in the answer and is not a condition precedent to be pleaded in the complaint as are other notice of claim statutes. Caruso v. Sloatsburg, 35 A.D. 2d 988, 317 N.Y.S. 2d 959 (2d Dep't 1970), construing §341-b of the Village Law analagous to the provisions contained in §2 of 3813 of the State Education Law.

Significantly, defendant BOARD in its reply to AETNA's amended answer, pleads no affirmative defense to AETNA's counterclaim.

In any event, it is highly questionable whether Section 3813 of the New York State Education Law applies at all in this instance. Since the charge of fraud is made against the BOARD, it would make no sense to require AETNA to give notice to the perpetrator of a fraud.

At trial, through the testimony of Mr. Fowler on cross-examination, commencing with page 636a of the transcript of trial and concluding with page 645a, and as substantiated by defendant AETNA's Exhibit "B" in evidence, unrefuted testimony was given supporting and providing the fraud perpetrated upon AETNA and the deliberate attempt to conceal the underlying facts and circumstances rendering this contract illegal.

Furthermore the concealment was not only as against AETNA, but certain members of the BOARD and the public as well. As testified to by Mr. Fowler, it never came out until the litigation ensued and the hearing was held before Judge McLean (645a). There was no objection upon the part of defendant BOARD to this testimony nor to the document, Defendant's Exhibit "B" in evidence.

The only purpose of the notice of claim is to notify the BOARD of the existence of the claim so that it can investigate into the facts. Rivero v. City of New York, 290 N.Y. 204, 48 N.E. 2d 486 (1943); State v. Waverly Central School District, 53 Misc. 2d 843, 280 N.Y.S. 2d 507 (1966); Newburg Nursery, Inc. v. Board of Ed. of Central School District §2, Towns of Ramapo, Orangetown, Clarkstown and Haverstraw, Rockland County, 41 Misc. 2d 997, 247 N.Y.S. 2d 74 (1964). In addition, there is no requirement that Section 3813 of the New York State Education Law - the law requiring the filing of notice of claim - must be strictly implied with. To the contrary, all that is required is "substantial" compliance. This was made abundantly clear in the case of Widger v. Central School District No. 1, 18 N.Y. 2d 646, 273 N.Y.S. 2d 72 (1966), where the plaintiff served a notice of claim on the School Board, alleging that the claim was for breach of contract and abuse of process. Plaintiff thereafter served a second amended complaint containing two

causes of action against the School Board, i.e., one styled in prima facie tort and the other for breach of contract. On appeal from an order denying a motion by the defendants to dismiss the complaint, the Appellate Division (23 A.D. 2d 811, 258 N.Y.S. 2d 195) held that the notice of claim was defective in part in that it in no way could be interpreted as giving the School Board notice that an action for prima facie tort was contemplated. The Court of Appeals reversed, stating that the notice of claim sufficiently informed the School Board of the nature of the claim, and that it complied with the provisions of Section 3813 of the Education Law, citing Rivero v. City of New York, supra. Also, see arbitration between Baker and Board of Education of Central School District #2 of the Towns of Bath, et al., 309 N.Y. 551, 132 N.E. 2d 837 (1956), where the Court stated that:

> "... All that is required is substantial compliance with the statute."

Since AETNA's claim for affirmative relief in fraud arises out of the very same set of facts which contributed to the basis of the fraud (i.e., the facts and circumstances surrounding the entering into of the contract), and was exclusively within the knowledge of the BOARD and concealed, there can be no justification for a contention by the BOARD that it was not apprised of the facts and could not investigate into them. To require the filing of a formal claim under these circumstances would be

ludicrous. Equity will not require the doing of a vain or useless thing or the performance of an impossible act. Margulis v. Messinger, 34 Misc. 2d 699, 210 N.Y.S. 2d 855 (1960).

POINT III

THE BOARD IS NOT ENTITLED TO RECOVER ANY DAMAGES

AETNA submits that defendant BOARD has totally failed to prove its entitlement to damages. The District Court on several occasions stated that the BOARD's claim of damages did not apply to additional defendant AETNA (690a and 692a), presumably because the equities were clearly in AETNA's favor.

In the pretrial order the defendant BOARD claimed $496,890.00 in damages (130a, 145a). On the first day of trial, counsel for defendant BOARD served a supplemental and amended answer to interrogatories, increasing its claim to $758,261.67.

Halfway through the trial, and after several days of direct and cross examination, the BOARD reduced its alleged claim of damages to ¶280,796.00 (672a) as set forth in a schedule which was admitted into evidence as defendant BOARD's Exhibit "99" (673a). Exhibit "99" has not been made a part of the BOARD's appendix for apparently obvious reasons. The BOARD now seeks an item of damages which it neither claimed in the pretrial order, or during the trial but as a

mere post-trial afterthought, namely, the claim of $170,000.00, representing the amount of the original change-order. The BOARD has suddenly become aware of its failure to prove damages. Counsel for the BOARD stated that these were the damages it was seeking and the BOARD was no longer asking for recovery back of the amount it had paid since it would be inequitable under Judge Ryan's decision (673a).

The BOARD's witness, Mr. Fowler, stated that the increased completion costs were $165,430.00 (668a), that he arrived at this figure by taking the figure of $2,429,476.00, which was the figure certified by the architect as being completed but not paid to plaintiff FABRIZIO, (668a), plus $428,164.00, cost of general construction of MARS-NORMEL, $102,017.00, cost of MacNamee, $29,329.00 cost of Bradhurst, plus $85,051.00 in re-letting disbursements and other payments, plus $9,349.00 for the alleged added cost of a clerk of the works and insurance, plus $21,358.00 in the architect's basic fee due to increases in construction costs for an alleged total construction cost of $2,807,127.00 (666a-667a). Included in that amount was a loss on retainage bonds in the sum of $5,103.00. The witness Fowler then testified that he deducted the $2,641,697.00 which represented all approved work by FABRIZIO and MARTIN including change orders resulting in an increased completion cost of $165,000.00 (668a). To this amount, the witness Fowler added interest on bonds he claimed the BOARD

was required to float in order to pay for the increased construction costs. The claimed interst amounted to $115,366.00.

(a) The damages the BOARD seeks are not the result of an illegal contract.

The only damages recoverable by the BOARD would be those damages which were a direct result or consequence of the illegal contract. Thus, damages, if any, would have had to be ascertained at the time of the contract. Any subsequent damages are irrelevant. First of all, the witness Fowler admitted that the next highest bidder was Walter A. Stanley & Company, whose bid was $250,000.00 higher (559a-560a). Thus, if the BOARD had not entered into the illegal contract, it would have entered into a contract with Walter A. Stanley & Company which would have cost $250,000.00 more. The illegal contract resulted in a savings instead of a loss. Also, the witness Fowler admitted that the increased construction costs it was seeking were the result of a breach of contract (527a). Furthermore, the plaintiff introduced into evidence on cross examination of the witness Fowler an architect's estimate of the cost of the work prior to the bidding. The architect's estimate for performing the work was $2,471,000.00, and was within a few thousand dollars less than the FABRIZIO contract for the general construction, plus alternates (Exhibit "5", 443a, 434a, 435a). However, this figure was above the base

bid price of FABRIZIO of $2,326,900.00, and the estimate was $200,000.00 above the Rand bid, who was the previous low bidder (434a).

In substance, the BOARD has attempted to do exactly what Judge Ryan said it could not do; i.e., recover damages for breach of contract and not such increased costs which the BOARD may have incurred by reason of the illegality involved.

Contrary to the BOARD's position, the illegality in and of itself raises no presumption of damage.

(b) There has been a total failure of proof by the BOARD of its claimed damages.

The first amount in the BOARD's computation of the $165,000.00 excess cost to complete was the contention that it had paid $428,164.00 to MARS-NORMEL, as completing contractor for general construction. The BOARD failed to introduce into evidence any such contract. The witness Fowler stated that the MARS-NORMEL contract was of a guaranteed maximum cost of $403,000.00 (481a). Through the witness Fowler, Exhibits "85A", "85B", "85C", "85D", "85E" and "85F" were introduced into evidence, which were the alleged requisition of payments totalling $428,164.80 (325a). However, the Court below advised counsel for the defendant

BOARD that these documents were being admitted subject to verification by furnishing the backup material (33a-334a). The BOARD's witness, Crane, from the architect's office, admitted that the requisitions of MARS-NORMEL did not contain the required backup and he could not verify the amounts in the requisitions which depended on the timeslips (784a-791a). The defendant BOARD never introduced into evidence these time slips. This is important because the BOARD claimed to have paid MARS-NORMEL amounts in excess of the $403,000.00 guaranteed maximum price for alleged extra work which could only be distinguished by an analysis of the time sheets. In addition, the MARS-NORMEL completion contract for construction was concededly different from the FABRIZIO and MARTIN contract (277a), and the differences were never shown by the BOARD. How can alleged payments under this contract be charged to FABRIZIO or be used as a basis for recovery of damages as against AETNA? The alleged MARS-NORMEL cost-plus contract also contained a savings clause of 50% (470a) making these items of cost especially relevant. Thus, the failure of the BOARD at the trial to show the component differences in the two contracts or the backup for the cost was a failure in the proof of its damages, since the contracts show what is a cost item. 10 N.Y. Jur., Contracts, §281.

Furthermore, the witness Fowler testified that the BOARD paid MARS-NORMEL $95,000.00 for masonry work under a subcontract

with John Barber & Sons, Inc., after the architect had certified in FABRIZIO's last requisition of February, 1966, that only $14,490.00 in masonry work remained (478a, 479a, and 480a). This was an $80,000.00 difference and certainly cannot be charged to FABRIZIO, ergo AETNA. Furthermore, the BOARD didn't even know whether MARS-NORMEL had paid the masonry subcontractor $95,000.00 for the work (486a) and proof of payment was not offered in evidence.

Similarly, the BOARD paid $47,500.00 to MARS-NORMEL for carpentry work when the last FABRIZIO requisition certified by the architect stated that only $28,950.00 in carpentry work remained (487a), a difference of $18,550.00. Again the witness couldn't testify whether MARS-NORMEL had paid $47,500.00 for the carpentry work (488a).

The BOARD further contended that it paid $25,164.00 above the guaranteed maximum price of $403,000.00, to MARS-NORMEL (321a, 491a), allegedly the result of a change order given to MARS-NORMEL (491a). The architect later determined that the additional items were FABRIZIO's responsibility (757a). However, the BOARD's witness stated and agreed that MARS-NORMEL's contract was for completion of FABRIZIO's work (321a, 491a). Thus, none of the additional items should have been paid for because it was FABRIZIO's obligation which MARS-NORMEL undertook to complete without extra compensation. Part of the alleged extra was $14,120.50 for punch list work above a $15,000.00 allowance in the MARS-NORMEL contract (498a).

However, nowhere in the record is there any backup of what the additional $14,120.50 in punch list work involved, and without the backup (time slips), the BOARD's own witness admitted he could not tell what these items involved (809a). In addition, the BOARD's own witness stated that because of mistakes in the bid documents prepared by the architect, MARS-NORMEL was given an extra (813a). Thus, the entire claim for extra work should be disallowed.

Furthermore, nowhere in the record is there any evidence of checks, etc., that supports the BOARD's contention that it in fact paid MARS-NORMEL.

Therefore, the BOARD failed to substantiate the payments to MARS-NORMEL. The contract was not introduced into evidence. No backup (time slips, etc.) were introduced into evidence on the cost-plus contract to establish cost. The BOARD's own records establish overpayments of $80,000.00 and $18,550.00. The BOARD paid $25,164.00 for extra work which was MARS-NORMEL's obligation under the completion contract, without backups and attributable to the architect's errors and mistakes. Thus, none of these items can be charged to the cost of completion.

The BOARD also contended that it paid two (2) other contractors to complete portions of FABRIZIO's work. The BOARD claimed that it paid MacNamee & Co. $102,017.00 and $29,329.00 to another contractor by the name of Bradhurst. Although

there were alleged contracts, none were introduced into evidence.

The BOARD's first witness stated that there were two contracts with MacNamee. The first was for $85,000.00 for roads and curbs and a second contract was on a cost-plus basis for $5,000.00 for miscellaneous undefinable items, that these contracts were negotiated by the BOARD and not publicly let (289a, 290a and 291a). The witness also testified that the Bradhurst contract was not publicly let and was for site work (290a, 291a).

In fact, it was later admitted by the BOARD's witness (Fowler, 627a) that there were two contracts with MacNamee; one for $62,046.22; the other a cost plus contract, originally estimated at $25,500.00 which ended up at $19,928.50 (627a). However, it was further admitted that an extra of $20,043.02 was given to MacNamee under the $25,500.00 contract and that neither the change order or the backup for the cost plus items or extra work could be found (795a-802a). Thus, the BOARD produced no substantiation for payments totalling $39,971.52. It should be noted that counsel for the BOARD was advised by the Court that the MacNamee requisitions were only being allowed into evidence on the proviso that verification would be produced either by backup material (time slips, etc.) or by the architect (333a-334a). The backup was not produced and the architect (Crane) testified

that he could only verify cost and extra work by time slips (789a-798a).

The Bradhurst payments allegedly totalled $29,329.00. The BOARD's witness stated Bradhurst was paid $5,400.00 on three change orders, and was unable to testify whether it was an item to be charged to FABRIZIO or not (522a). The BOARD never substantiated the Bradhurst payments with backup and its own witness admitted he did not have the substantiation (Crane, 788a-789a).

The BOARD's own witnesses testified that the BOARD entered into direct contracts with Bradhurst and MacNamee without public bidding (647a). The BOARD's witness also admitted that the BOARD had only approved contracts with MacNamee and Bradhurst not to exceed $117,500.00, and in fact, the combined contracts totalled $131,000.00 (742a).

In addition, Mr. Fowler admitted that he had spoken to Charles Brind, counsel to the Commissioner of Education, and had written a memo to the BOARD's attorney, Mr. Yavner, concerning competitive bidding requirements (Defendant AETNA's Exhibit "C" in evidence (646a). On page 651a, Mr. Fowler stated that he followed category "C" of Exhibit "C" in entering into the contract with Bradhurst and MacNamee (651a).

Category "C" states:

> "If the School District chose to assume the work of the contractor itself and to employ the subcontractor already employed by

> Fabrizio and Martin to finish the job, together with the other tradesmen not provided under a subcontract, then we would not be subject to the bidding Law."

The record is clear that the BOARD did not assume the work of the contractor since it was MARS-NORMEL who became the contractor. Thus, the MacNamee and Bradhurst contracts were not pursuant to the bidding laws, General Municipal Law, §103. See also: Application of Gottfried Baking Company, 45 Misc. 2d 708, 257 N.Y.S. 833 (S. Ct., Albany Co., 1964); Application of Glen Truck Sales & Service, Inc. v. Sirignano, 31 Misc. 2d 1027, 220 N.Y.S. 2d 939 (S. Ct., West. Co., 1961). It is submitted that the alleged damages attributable to the MacNamee and Bradhurst contracts flow from an illegal contract and cannot be used as a basis of recovery in this suit. Certainly on equitable principles, these damages should be rejected and no recovery permitted.

Of note is the fact that all the damages sustained by the BOARD were unnecessarily incurred because the testimony is clear that the additional defendant AETNA was willing to financially support FABRIZIO to complete the work without any expense to the BOARD (870a-874a).

Another item of damage claimed by the defendant BOARD was the sum of $85,051.00 for various miscellaneous expenses. Included in this item, were bills for Port-O-San toilets, which the BOARD's own witnesses admitted were MARS-NORMEL's responsibility (426a), and therefore should have not been paid

for by the BOARD. Included in that sum was overtime for secretaries. However, the witness was unable to testify as to what the secretaries were doing (427a-429a). The BOARD claimed charges for guards to protect the premises which it claimed was FABRIZIO's responsibility and after MARS-NORMEL was on the job on April 12, 1966, admitted that it was MARS-NORMEL's responsibility, yet continued to pay the bills (431a). The BOARD included charges for legal services but failed to show how this was an item of cost (432a). They admitted that items such as the cost of sandwiches, photographs, etc., were included items (705a). The BOARD's witness (371a-382a) stated that the BOARD had made the payments listed in the schedule, but failed to substantiate these charges as items of cost of completion and didn't know what the payments were for and failed to submit any evidence of payment. Furthermore, the witness Mr. Fowler, was not qualified to testify that these were items of cost to complete. All he was qualified to state was that these were items paid since he was merely an administrator. Only the architect was qualified to so testify and there is no such testimony in the record.

Another item included in the BOARD's damage was a claim of $1,800.00 for alleged additional insurance. However, the BOARD's witness stated that he didn't know the policy period or for what period the premiums were applicable (417a). Further, there was evidence by the BOARD that it was a three-

year policy which was from July 1, 1964 to July 1, 1967, and there was only one (1) payment made (592a). Thus, it made no difference that the contract time ran over, since the policy was already paid.

In addition, the BOARD claimed an additional $21,358.00 in architect's fees because it claimed that there were additional construction costs (668a-669a). However, the BOARD failed to establish the additional construction cost as being chargeable to FABRIZIO and thus the additional fee is not substantiated. Further, Mr. Fowler testified that the alleged architects were not licensed to practice in New York State (416a). As such, the architects were not entitled to any fees. 2 N.Y. Jur. Architects, §26. Thus, any payments made by the BOARD were strictly voluntary and cannot be charged to FABRIZIO.

Furthermore, throughout the trial, the BOARD's testimony was that the architect certified everything, and that the witness Crane was from the architect's office. Any testimony from Mr. Crane has dubious worth and, in fact, there were no architects certified since one is not deemed an architect until you are licensed as such.

The final item of damage claimed by the BOARD was interest in the sum of $115,366.00 as the cost for the notes and bonds it was alleged had to be sold to finance the cost of completion. This figure was based on an alleged cost to complete of

$165,430.00. The BOARD is not entitled to this sum for numerous reasons. First of all the BOARD has not established that its cost of completion was $165,430.00. To the contrary, the BOARD has failed to establish any excess cost to complete. Another reason is that the bonds were not sold to finance completion costs. Mr. Fowler who was the main witness on this point by the BOARD continued to insist that this was the reason. Mr. Fowler was shown a memo he wrote dated April 12, 1966, and which was admitted into evidence as defendant's Exhibit "A" (635a). Mr. Fowler admitted that this memo was written after the completion bidding (633a). This memo was entitled "$250,000.00 in Additional Bonds Required for Completion of the Middle School." Mr. Fowler on page 4 summarized the need for the bonds and in subparagraph (6)(g) stated:

> "Members of the Board acting in good faith, had every intention prior to the default of Fabrizio & Martin of seeking informal approval of the voters in this matter (Public Statement of The Board President as an individual on March 2, 1966)."

Also, on page 2 of that same memo defendant's Exhibit "A" in evidence, Mr. Fowler stated that part of the bond money for the equipment of the school had been used in extra rock excavation during the time FABRIZIO was on the project. In other words, Mr. Fowler contradicted his own memo in his testimony. Fowler repeatedly stated that the bond issue was required because of the construction cost to complete. However, it is clear that the bond issue was contemplated prior

to any alleged default. The default is only being used as an excuse to charge someone else for the financing cost of the bonds.

Furthermore, interest on bonds would not be a recoverable item of damage for alleged completion costs. The only interest the BOARD would be entitled to would be any legal rate of interest which would normally be awarded on any recovery of damages. It is punitive to require FABRIZIO to pay for thirty years of interest on bonds.

CONCLUSION ON BOARD'S DAMAGES

The BOARD's failure to introduce the contracts of MARS-NORMEL, Bradhurst and MacNamee into evidence precludes the BOARD from testifying as to the cost to complete. The best or primary evidence were the contracts and secondary evidence an only be permitted when the primary evidence is not available. Taft v. Little, 178 N.Y. 127 (1904). Therefore, the testimony of the BOARD's witnesses which was permitted over objection concerning the completion contracts should be disregarded.

Furthermore, all of the BOARD's Exhibits "85A" through "90F" which are not part of the BOARD's appendix were introduced into evidence, subject to verification, which was the backup (time slips, etc.). The backup was never produced. Therefore, any claim of payments to MARS-NORMEL, Bradhurst and MacNamee should

not to be considered.

The BOARD failed to show that the completion costs were fair and reasonable. To the contrary, there was evidence that the charges were reckless and extravagant and thus should not be charged to FABRIZIO. In determining the reasonable cost of completion it was necessary for the BOARD to determine first what work was actually performed by the plaintiff FABRIZIO and what remained to be completed after the alleged termination. There was a total failure of proof by the BOARD as to the reasonableness of its cost of completion and what work remained to be done and thereby precluding the BOARD from recovering its alleged damages which are speculative at best. Clark v. Fleischmann Vehicle Co., 187 N.Y.S. 807, 813 (S. Ct. N.Y. Co., 1921).

Furthermore, the BOARD claimed the payment of certain sums for the completion of the school buildings after the FABRIZIO termination. The payment of these amounts does not prove the value of the unfinished work which the BOARD was entitled to deduct from the contract price or charge FABRIZIO because the mere fact of payment, standing alone, is not sufficient evidence of value. Kennedy v. McKone, 10 App. Div. 88, 41 N.Y.S. 782 (1st Dep't 1896).

All of the foregoing, in any event, constitutes proof as to damages for breach of contract and not damages resulting from the illegality of the contract.

POINT IV

DAMAGES ARE NOT PRESUMED IN AN ILLEGAL CONTRACT

The BOARD in Point I, Point III and Point IV of its brief argues that because the contract is illegal, presumptively it is entitled to damages under Gerzof v. Sweeney, 22 N.Y. 2d 297, 292 N.Y.S. 2d 640 (1968). This is not so. The BOARD in Points III and IV of its brief claims that it is entitled to recover back the $171,000.00, the amount of the illegal change order. Also, the BOARD claims that it is entitled to recover back the $3,000.00 (Point IV) representing the excess payment on Alternate No. 3.

The BOARD did not in the pretrial order (130a), claim the $171,000.00 or $3,000.00 as an item of damage. The BOARD did not claim the $171,000.00 or $3,000.00 as an item of damage in its amended schedules of damage. The BOARD's own schedule of damage (Exhibit 98, 1051a) did not claim the $171,000.00 or $3,000.00 as an item of damage. The BOARD's own Exhibit 99 which it failed to annex to the appendix did not claim the $171,000.00 or the $3,000.00.

In Gerzof, (supra), the Court held at page 646 that the public bodies entitlement to damages was measured by the difference between the price the Village received and the next lowest bidder. In the instant case, the next bidder exceeded FABRIZIO's price by $222,100.00. The BOARD suffered

no damages because of the illegality. To the contrary, the illegality saved the BOARD money. The next highest bidder since Rand Construction Co., the lowest bidder, had been released from its bid due to a mathematical error (83a) was Walter Stanley Construction Co., whose bid was $222,100.00 higher than FABRIZIO's bid. Thus, if the change order of $171,000.00 was added to the FABRIZIO bid, the BOARD would still have been required to pay an additional $51,100.00.

In addition, the BOARD's own Exhibit 98 (1051a) states that at the time of the termination of the contract, FABRIZIO had earned $2,641,697.00, had been paid only $2,126,756.00 leaving a difference of $514,941.00, which the BOARD kept as a forfeiture because the contract was declared illegal. The amount far exceeds the $171,000.00. In addition, the BOARD has successfully avoided payment to FABRIZIO for services, labor and materials in the sum of $708,526.15 (1070a).

In Gerzof (supra), the Court of Appeals determined that there could be circumstances where equity must intervene to prevent the usual harsh penalties of complete forfeiture by the contractor when the competitive bidding statutes have been violated. (Gerzof, supra, p. 645) Thus, under Gerzof, the trier of fact should fashion an equitable remedy while still vindicating the public bidding statutes. In Gerzof (supra), and subsequent decisions of the New York Courts,

the equitable principle was determined by the degree of wrong committed by the contractor.

In Gerzof (supra), the contractor actively participated in rigging the specifications so that there could be no other bidders. The remedy fashioned was that the contractor had to pay back the difference between the lowest bidder and what the contractor had bid.

In S. T. Grand, Inc. v. City of New York, 32 N.Y. 2d 300, 344 N.Y.S. 2d 938 (1973), the contractor had bribed a public official in order to get the contract. In Grand, (supra, 943, 944), the Court of Appeals held that the equitable remedy fashioned in Gerzof (supra), was not available to the contractor because there had been bribery of a public official which required the harshest penalty of all -- complete forfeiture.

In Jered Contracting Corp. v. New York City Transit Authority, 22 N.Y. 2d 187, 292 N.Y.S. 2d 98 (1968) decided eight (8) days before Gerzof (supra), there was a question of whether there had been collusive bidding and whether such a defense could be raised. The Court of Appeals held such a defense to be valid and remitted the case for further proceedings. Sufficient facts were not before the Court so it could fashion an equitable remedy.

In the instant case, FABRIZIO was a Connecticut contractor who had originally bid the project in compliance with

the Public Bidding statutes (82a). Due to circumstances, the lowest bidder Rand Construction Co. was permitted to withdraw its bid because Rand had made a mistake in its bid, leaving FABRIZIO the next lowest bidder. But FABRIZIO had also made a mathematical error (83a) and requested leave to withdraw its bid. The BOARD was completely satisfied with the fact that FABRIZIO had made an error and Judge McLean so found (84a). Thus, like Rand, FABRIZIO too could have been released from its bid. Moffett H. & C. Co. v. Rochester, 178 U.S. 373, 20 S. Ct. 957, 44 L.E. 1108 (1900). There is no question that FABRIZIO was seduced into entering into the contract on the representations of the BOARD and its counsel that everything was proper and legal (85a-86a). The BOARD well knew that there were grave questions concerning the legality of the contract and deliberately attempted to conceal by removal and destruction of public records (83a, 642a), all the evidence to prove the illegality. The BOARD never advised FABRIZIO that there were grave questions of legality so that FABRIZIO could seek the advice of counsel. Instead, the BOARD entrapped FABRIZIO into thinking everything was legally proper.

Under the circumstances, what should be the equitable remedy fashioned by this Court? Did Judge Ryan fashion an equitable remedy in holding that FABRIZIO could not recover its contract balance (96a)? Did the Court below, as the trier of the facts, fashion an equitable remedy by leaving the parties

where they are since it concluded that the BOARD lost nothing as a direct consequence of the illegality and that the contractor was punished severely and harshly by losing the right of recovery and forfeiting its contract balance of $514,941.00?

AETNA submits that by reason of the facts in the instant case this Court should follow the more moderate rule as set down in Blum v. City of Hillsboro, 49 Wis. 2d 667, 183 N.W. 2d 47 (1971) and allow FABRIZIO a recovery of his actual costs without overhead and profit. Certainly, this would be equitable, and would at the same time continue to discourage illegal contracts and impose a not unfair burden on the contractor.

POINT V

THE TRIAL COURT CORRECTLY EXCLUDED ANY EVIDENCE OF STATE ACTIONS BROUGHT BY ALLEGED PRIME CONTRACTORS AND SUBCONTRACTORS AGAINST BOARD

At the very outset, a totally untrue and misleading statement by the BOARD must be corrected.

At page 44 of the BOARD's brief, it is stated that in consideration of the BOARD's forebearance to sue, AETNA agreed to assume the obligations to defend the BOARD against prime contractor suits in the supplemental agreement. This totally false statement is not only unsupported by any evidence but the supplemental agreement (1036a-1049a) is completely devoid of any such statement or representation. Again, the BOARD attempts to plead and prove a supplemental agreement which

Ryan, J. has held cannot be pleaded or proved (118a).

The BOARD neglects to state that the subcontractor claims the BOARD now seeks to hold AETNA responsible for were dismissed as against AETNA in the state courts (902a, 906a, 912a). As a matter of fact, one of the subcontractors, Bradhurst, was one of the BOARD's completing contractors who might be suing for the failure of the BOARD to pay completion costs.

The Trial Court was correct in excluding the alleged claims by prime contractors for delays. First of all, any claims would be speculative. Secondly, the delay damages would be a result of a breach of the BOARD's duty to the prime contractors and not FABRIZIO's. Furthermore, delay damages are not a direct consequence of the illegality.

It was stated in Shalman v. Board of Education of Central School District No. 1, 31 A.D. 2d 338, 297, N.Y.S. 2d 1000, 1003 (3rd Dep't. 1969).

> "...A duty is imposed upon the employer not to interfere with the prosecution of the work of his contractor, and he impliedly agrees that the contractor will not be unreasonably delayed by the failure of other contractors to perform work which is essential to the performance of the work in question. (Sundstrom v. State of New York, 213 N.Y. 68, 106 N.E. 924; 10 Encyclopedia New York Law, Op.Cit., §565). For a breach of that duty the contractor may recover his resulting damages. (10 Encyclopedia New York Law, Op. Cit., §565)..."

10 Encyclopedia New York Law, Impeding or Delaying Progress of Contractor, §565, page 19 states:

> "A duty is imposed on the employer not to interfere unreasonably with the due prosecution of the work undertaken by the contractor, and there is also an implied agreement on his part that the contractor will not be unreasonably delayed in his work by the failure of other contractors to perform work which is essential to the doing of the work in question, and for a breach by the employer in this respect the contractor may recover his resulting damages; he is not required when so delayed to abandon the work and sue for general damages as for a final breach of the contract, and as a general rule the damages recoverable for such interference are the enhanced cost of doing the work. Accordingly, where, due to an increase in the cost of labor and materials, the cost of performing the contract is enhanced, such increased cost is recoverable by the contractor, and the same is true where on account of the delay the contractor is forced to do the work at a more unfavorable season of the year and consequently at an additional cost."

Furthermore, the trial court found that the delays caused on the project were the fault of the BOARD:

> "***The Board was slow in paying the monthly requisition which the contract called for. It delayed executing change orders with promptness and failed to make payments for work completed as prescribed and refused to allow extensions when extra work was required. * * *"(1057a)

Thus, it is clear that the alleged delay damages sought by the prime contractors were solely the fault of the BOARD for which FABRIZIO and AETNA are not responsible.

CONCLUSION

THE EQUITIES ARE CLEARLY IN AETNA'S FAVOR VIS-A-VIS THE BOARD AND THE BOARD'S COUNTER-CLAIMS WERE PROPERLY DISMISSED AS AGAINST AETNA.

THE TRIAL COURT ERRED IN DENYING AETNA RECOVERY FOR DAMAGES IN THE SUM OF $193,227.19 SUSTAINED AS THE RESULT OF THE FRAUD PERPETRATED BY THE BOARD AFTER CONCLUDING THAT THE BOARD FAILED TO DISCLOSE MATERIAL FACTS.

THE TRIAL COURT WAS CORRECT IN HOLDING THAT THE BOARD SUFFERED NO DAMAGES AS A CONSEQUENCE OF THE ILLEGALITY. THE NEXT LOWEST BIDDER FOR THE SAME PROJECT EXCEEDED THE $171,000.00 BY $51,100.00 AND THE BOARD RETAINED THE BENEFIT OF $708,526.50, THE UNPAID VALUE OF LABOR AND MATERIALS FURNISHED BY FABRIZIO. DAMAGES FOR BREACH OF CONTRACT AND COSTS OF COMPLETION WERE NOT A CONSEQUENCE OF ILLEGALITY BUT WERE A RESULT OF THE BOARD'S OWN BREACHES OF CONTRACT AND MISCONDUCT.

THE SUITS IN STATE COURT BY THE OTHER PRIME CONTRACTORS AND SUBCONTRACTORS WERE PROPERLY EXCLUDED SINCE THE SUBCONTRACTOR'S SUITS WERE PREVIOUSLY DISMISSED AS AGAINST AETNA. THE PRIME CONTRACTORS' SUITS FOR DELAY ARISE OUT OF BREACH OF CONTRACT BY THE BOARD AND ANY CLAIM FOR DAMAGES WOULD BE SPECUALTIVE.

Respectfully submitted,

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DAVID A. TRAGER,
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On the Brief.

In the
United States Court of Appeals
for the Second Circuit

376—Affidavit of Service by Mail The Reporter Co., Inc., 11 Park Place, New York, N. Y. 10007

Fabrizio & Martin
Plaintiff-Appell-Appellant
vs.
Board of Education Central School District No.2 of the Towns of Bedford, New Castle North Castle et al.
Defendants

State of New York, County of New York, ss.:

Raymond J. Braddick, agen for Max E. Greenberg, being duly sworn deposes and says that he is the attorney for the above named Additional Defendant-Appellee herein. That he is over 21 years of age, is not a party to the action and resides at 8 Mill Lane Levittown, NY

That on the 28th day of August, 19 74 he served the within Brief and Exhibit Volume

upon the attorneys for the parties and at the addresses as specified below

1. Louis E. Yavner Esq.
Atterney for Defendant Beard of Education
60 East 42nd. Street
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by depositing 2 copies of Brief to each, and 1 copy of Exhibit Volume to each to each of the same securely enclosed in a post-paid wrapper in the Post Office regularly maintained by the United States Government at
90 Church Street, New York, New York
directed to the said attorneys for the parties as listed above at the addresses aforementioned,

that being the addresses within the state designated by them for that purpose, or the places where they then kept offices between which places there then was and now is a regular communication by mail.

Sworn to before me, this 28th.

day of August, 1974

ROLAND W. JOHNSON
Notary Public, State of New York
No. 4607705
Qualified in Delaware County
Commission Expires March 30, 1975